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BEFORE THE ARIZONA CORPORATION
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Arizona Corporation Commission

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EXCEPTION

APR 9 1999

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) DOCKET NO. RE-00000C-94-0165

IN THE MATTER OF THE COMPETITION IN
THE PROVISION OF ELECTRIC SERVICES
THROUGHOUT THE STATE OF ARIZONA.

)
) TUCSON ELECTRIC POWER
) COMPANY'S SUPPLEMENT TO
) EXCEPTIONS TO PROPOSED
) AMENDMENTS TO DECISION NO.
) 60977

Tucson Electric Power Company ("TEP" or "Company"), through undersigned counsel,
hereby submits this supplement to its Exceptions to Proposed Amendments to Decision No. 60977
("Exceptions"), that was submitted to the Commission on February 17, 1999, as follows:

1. INTRODUCTION.

By way of this supplement, TEP brings to the Commission's attention additional analysis
that supports TEP's position that it has a right to a legitimate opportunity to recover 100 percent of
its stranded costs. As TEP pointed out in its Exceptions, the Proposed Amendments will not
provide TEP with that opportunity. TEP is supplementing its Exceptions at this time because it has
recently researched additional cases that have a direct bearing on the stranded cost issue and
should be considered by the Commission.

2. THE U.S. SUPREME COURT'S HOLDING IN Russell v. Sebastian .

TEP has steadfastly maintained that it has a right to be fully compensated for the taking of
its property, including its exclusive CC&N, as a result of the Commission-ordered transition from
a monopoly to a competitive market scheme. In this vein, TEP has presented to the Commission
exhaustive analysis and research regarding the Regulatory Compact, the nature and scope of

1 TEP's exclusive CC&Ns, and legal standards for unlawful confiscation, just compensation and
2 stranded costs. Other parties and intervenors have weighed in on these issues and have presented
3 their analysis to the Commission. However, until now no party has presented to the Commission
4 the United States Supreme Court's decision in Russell v. Sebastian, 233 U.S. 195 (1914).

6 In the Russell case, the U.S. Supreme Court reversed and remanded the decision of the
7 California Supreme Court to deny habeas corpus relief to a utility employee who had been arrested
8 for excavating in a city street for the placement of utility mains, without a prior municipal license,
9 contrary to a municipal ordinance.

11 Russell was an employee of the Economic Gaslight Company (the "EGC"). EGC first
12 provided gas to the City of Los Angeles pursuant to California Constitution, Art. 11, Sec. 19
13 (1885) (the "Constitutional Provision"), which permitted an individual or company to use the
14 public streets for laying down pipes and conduits for introducing and supplying gaslight, other
15 illuminating light and water, where there were no public works owned by the municipality.

18 The Constitutional Provision was amended, and the City enacted an ordinance that required
19 EGC to first obtain written permission from the City's board of public works in order to excavate
20 in a street. EGC applied for the permission but was told that in order to excavate it would first
21 have to obtain a franchise by purchase. EGC did not, informed the City that it would proceed to
22 excavate, and asked the City to supervise the excavation. The City arrested the excavator, Russell.
23 Russell then sought habeas corpus to be freed on grounds including that the municipal legislation
24 impaired EGC's contract with the state in violation of article I, § 10, of the Federal Constitution.

27 The Court analyzed the Russell case utilizing **contract principles**. The Court determined
28 that the Constitutional Provision constituted an **offer** to which the state was bound upon EGC's
29 acceptance:
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31 That the grant, resulting from an acceptance of the state's offer,
constituted a contract, and vested in the accepting individual or
corporation a property right, protected by the Federal Constitution,

1 is not open to dispute in view of the repeated decisions of this
2 court. Id. at 204.

3 The Court then analyzed the Constitutional Provision as it would any contractual offer to
4 determine its scope and breadth. It further analyzed the practical circumstances and intent of the
5 contract to determine how acceptance of the contract was to be demonstrated. Then the Court
6 applied the undisputed facts to its contractual analysis to determine that the EGC's acceptance of
7 the offer was complete. The Court concluded that neither the amendment of the Constitutional
8 Provision nor the City's ordinance was permitted to interfere with EGC's existing contract right.
9 Consequently, the Court held that the State's actions constituted a contract, and vested in the
10 accepting individual or corporation a property right, protected by the Federal Constitution.
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12 EGC's compact with the City of Los Angeles (as authorized by the California Constitution)
13 created a contract and bestowed upon EGC property rights. Clearly, the plant that EGC had
14 acquired and constructed became "stranded" as a result of the City of Los Angeles' change in
15 municipal ordinances and at the point when EGC was prohibited from further extension of or
16 addition to the existing water distribution system. It is important for this Commission to consider
17 and follow the US Supreme Court's ruling based upon contract principles in the Russell case
18 because it is analogous to TEP's situation.
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20 TEP accepted the State of Arizona's offer to provide exclusive electric service within a
21 geographic area when it received its CC&N. TEP took upon itself the responsibility of investing
22 in sufficient infrastructure to ensure that economic, safe and reliable electric service is available to
23 all current and future customers who request it. The Commission's Competition Rules, like the
24 revised City of Los Angeles ordinance, changes (and, therefore, interferes with) the contract
25 entered into between TEP and the State of Arizona. Because that contract vested in TEP as "the
26 accepting individual or corporation a property right, protected by the Federal Constitution" it must
27 be compensated for any taking of all or any portion of that right. As stranded cost recovery is the
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1 mechanism that the Commission has elected as the means whereby TEP will be compensated for
2 the transition to a competitive marketplace, it follows that TEP must have a legitimate opportunity
3 to recover 100 percent of its stranded costs. Because the Stranded Cost Recovery Options 1, 2 and
4 3 of the Proposed Amendments to Decision No.60977 do not provide for such an opportunity, they
5 should not be adopted in their present form by the Commission.
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8 **3. THE U.S. COURT OF APPEALS HOLDING IN Public Service Co. of New**
9 **Hampshire v. Patch.**

10 In Public Service Company of New Hampshire, No. 98-1764, 1998 WL 823177 (1st Cir.
11 Dec. 3, 1998)(“PSNH”), the First Circuit Court of Appeals affirmed the district court’s preliminary
12 injunctions enjoining the New Hampshire Public Utility Commission (“NH Commission”) from
13 requiring any utility to comply with the NH Commission’s plan (“Plan”) to deregulate electric
14 utility industry.
15

16 PSNH is the largest electric utility in New Hampshire, supplying about seventy percent of
17 the retail electric power in the state. PSNH filed for bankruptcy protection in 1988 due to
18 extensive delays and cost overruns in construction of a nuclear generating plant. The State of New
19 Hampshire intervened in the bankruptcy proceedings. Northeast Utilities agreed to acquire all of
20 PSNH’s stock and its nuclear generating plant. As a part of PSNH’s reorganization plan, the State
21 executed a rate agreement to permit Northeast Utilities to recover its investment. The rate
22 agreement contained formulas for allocating the recovery of the investment, including the nuclear
23 generating plant, over time to distribute the impact on retail rates. The bankruptcy court approved
24 the reorganization plan and the rate agreement. The New Hampshire legislature and the NH
25 Commission also approved the rate agreement. But in 1996, the New Hampshire legislature
26 adopted legislation providing for the introduction of competition into the electric utility industry in
27 New Hampshire.
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1 Under the 1996 legislation, the New Hampshire Commission adopted the Plan, which
2 included a provision for utilities to recover their investment in existing plant, but as PSNH alleged,
3 “cast doubt” on the utilities’ ability to recover their prudent investment in distribution,
4 transmission, and generation facilities. As a result, PSNH filed a 13-count complaint in federal
5 district court and requested a temporary restraining order against implementation of the Plan.
6 PSNH submitted affidavits of experts explaining that the Plan could ultimately force PSNH back
7 into bankruptcy. The Commission did not show that the experts’ analysis and projections were in
8 error. As a result, the First Circuit determined that the Plan was likely to inflict irreparable harm
9 on PSNH.
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12 PSNH argued that the Plan was preempted by specific provisions of the Federal Power Act,
13 the Public Utilities Regulatory Policies Act of 1978, and the Public Utility Holding Company Act.
14 The district court issued an order enjoining the implementation of the Plan. The district court
15 considered arguments on both ripeness and abstention issues, but denied those defenses of the
16 Commission, which then appealed. With respect to the ripeness argument, it was argued that
17 because the Commission was conducting ongoing proceedings with the potential of refining the
18 Plan, the Court should postpone its review of the Plan. This is similar to arguments that parties
19 have made regarding this Commission’s proceedings in this and related dockets.
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22 On appeal, the First Circuit considered ripeness; that is, whether the case was premature, by
23 analyzing (1) whether the issues were fit for review and (2) the hardship to the litigant in
24 postponing judicial intervention. The First Circuit expressly stated that the concurrent state court
25 proceeding did not render the federal case unripe because PSNH’s federal constitutional claim
26 under the Contracts Clause would not necessarily be resolved by the state court.
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29 With respect to the abstention issue, the First Circuit focused on the doctrine’s purpose “to
30 prevent federal courts from bypassing a state administrative scheme and resolving issues of state
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1 law and policy that are committed in the first instance to expert administrative resolution.” Id. at
2 *8. But this doctrine “does not bar federal court injunctions against state administrative orders
3 where there are predominating federal issues that do not require resolution of doubtful questions of
4 local law and policy.” Id. The First Circuit held that the abstention doctrine did not apply here
5 because the claims did not require specialized knowledge beyond the express provisions of the
6 Plan. The court also held that an older form of the abstention doctrine did not apply here.
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9 On or about July 16, 1991, various creditors of TEP filed Involuntary Petitions for
10 reorganization of the Company (Chapter 11) with the United States Bankruptcy Court for the
11 District of Arizona (“Bankruptcy Court”). On October 11, 1991, the Commission entered Decision
12 No. 57586 which established interim rates and charges to be collected by TEP. On December 31,
13 1991 the Commission entered Decision No. 57674 which made permanent the rates authorized in
14 Decision No. 57586. The Bankruptcy Court dismissed the involuntary petitions in reliance upon,
15 inter alia, the permanent rates set by the Commission in Decision No. 57674. The Commission’s
16 Competition Rules and the Proposed Amendments to Decision 60977, like the New Hampshire
17 Plan, “cast doubt” on TEP’s ability to recover its prudent investment in distribution, transmission,
18 and generation facilities. This Commission should recognize that, in Arizona, TEP is in a unique
19 position based upon the reliance of the Bankruptcy Court, TEP’s creditors and shareholders to the
20 Commission’s Decision No. 57674. To jeopardize the rate relief that was ordered in Decision No.
21 57674 (and subsequent TEP rate case orders) would be contrary to the terms and conditions that
22 were presented to and relied upon the Bankruptcy Court in dismissing the Involuntary Petitions.
23 As the Court of Appeals held in the PSNH case, this could cause irreparable harm. That is the last
24 type of activity or conduct that this Commission should be involved in. Instead, this Commission
25 should be striving to serve the public’s best interest. To the extent that the Proposed Amendments
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1 create uncertainty and doubt with regards to the rate relief that this Commission ordered and the
2 Bankruptcy Court relied upon, they do not serve the public interest.

3
4 **4. CONCLUSION.**

5 The cases discussed in this supplemental filing are important and shed additional light on
6 the proper solution to the transition from a monopoly system to a competitive marketplace. These
7 cases strongly support TEP's position that it has a property right in its CC&N, that this right is the
8 result of the Regulatory Compact and that it is entitled to full compensation when that right is
9 taken in part or in whole. Moreover, based upon the Commission's Decision No. 57674 (and
10 subsequent TEP rate case orders), any detrimental impairment to TEP's ability to recover the rates
11 set therein would be irreparable and subject to injunctive restraint.
12

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14 RESPECTFULLY SUBMITTED this 9th day of April, 1999.

15
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24 this 9th day of April 1999, to:

25 The Distribution List for Docket No. RE-00000C-94-0165

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